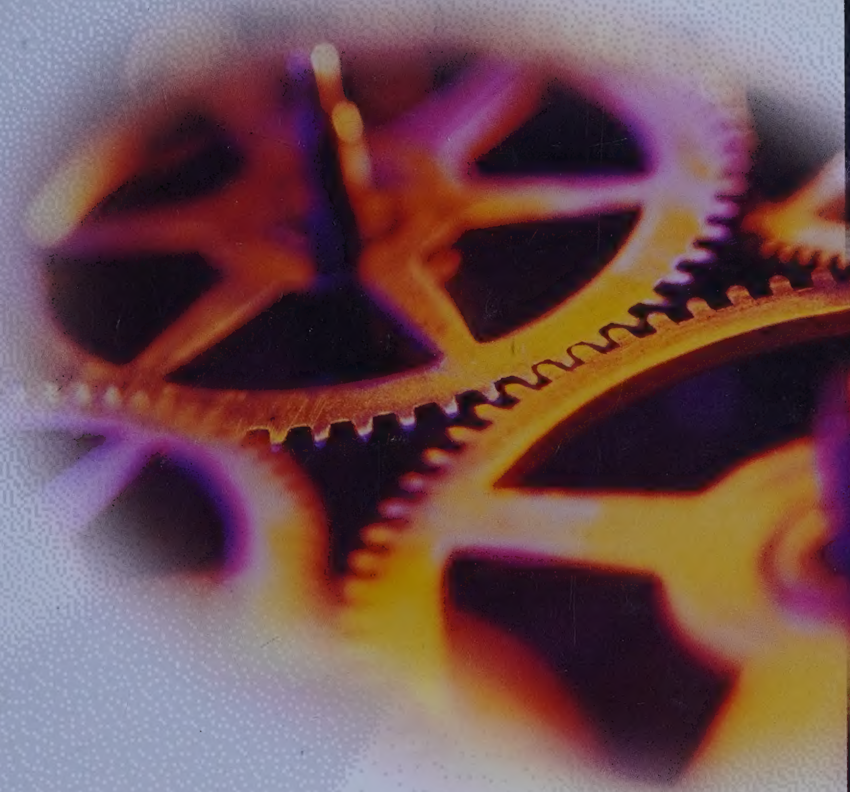


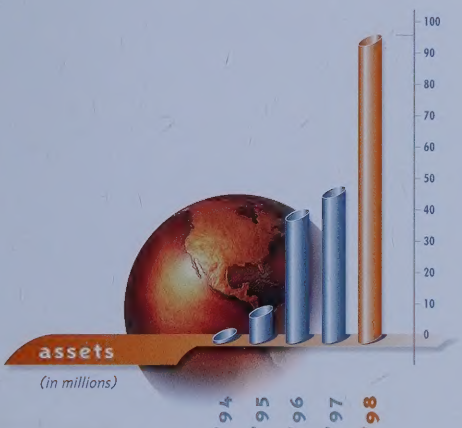
annual report 1998

ARCHITEL

company profile

Architel Systems Corporation is a leading provider of Operations Support Systems to the global telecommunications industry. Architel's products support the total provisioning needs of telecommunications service providers world-wide. Founded in 1984, Architel currently has over 420 employees and has licensed its products to over 40 customers world-wide. The Company has established a reputation for product innovation, technical excellence and customer delivery that provides it with a significant competitive advantage. Architel is a leader in its industry and is providing some of the indispensable building blocks that will enable the transformation of the global telecommunications industry. The Company operates from headquarters in Toronto, Canada as well as from offices throughout the United States and Europe. Architel's stock trades on the Toronto Stock Exchange under the symbol "ASY" and on the NASDAQ Stock Market under the symbol "ASYCF".

financial highlights



	1998	1997
INCOME STATEMENT		
Revenues	**$ 50,775,182**	$ 33,034,436
Net Income	**2,320,776**	4,225,847
BALANCE SHEET		
Current Assets	**$ 56,921,776**	$ 43,318,793
Capital Assets	**5,701,595**	3,562,392
Intangibles	**32,359,664**	–
Other Assets	**731,120**	528,180
Total Assets	**$ 95,714,155**	$ 47,409,365
Current Liabilities	**17,066,332**	6,867,937
Total Liabilities	**$ 17,066,332**	$ 6,867,937
SHAREHOLDERS EQUITY		
Total equity	**$ 78,647,823**	$ 40,541,428
(Number of Employees)	**414**	211

Financial information in this report is expressed in Canadian dollars, unless otherwise stated.

to our shareholders

The employees of Architel Systems Corporation excelled in 1998. Yet again, we recorded record financial results in a year in which we completed our first acquisition, significantly broadened our product portfolio and expanded our operational capability on a global basis. Through these actions we positioned ourselves to provide a comprehensive product solution to address the total provisioning needs of communications providers around the world.

Once again, our customers challenged us as they continued to experience dramatic change. We rose to the challenge and successfully expanded our customer base and delivered world-class product solutions to start-ups, ILECs, CLECs, PTTs, ISPs, RBOCs, IXCs, wireless providers and cable companies. Architel is clearly viewed as a leader in the Operations Support Systems market and we embrace the opportunity to help our customers prosper in the rapidly changing world of telecommunications.

THERE WERE MANY HIGHLIGHTS IN 1998 OF WHICH THE FOLLOWING DESERVE SPECIAL MENTION:

ACQUISITION OF ACCUGRAPH

During the third quarter we announced and closed the acquisition of Accugraph Corporation. Accugraph, a leader in the area of network planning and provisioning, and Architel had successfully teamed on a number of CLEC opportunities and it was clear that by combining the product offerings of the two companies, we could create a unique solution in the industry, unmatched by our competitors. We moved swiftly to consolidate all operational groups and office infrastructure, reorganized the executive team to take advantage of the strengths of both companies and successfully delivered a record fourth quarter, the first to be reported on a consolidated basis. Post acquisition, we successfully sold Accugraph products to Architel customers and proved the synergy of the product portfolio. However, the ultimate recognition of the success of this acquisition was the signing of a $20 million (US) contract with a very high profile CLEC in the United States market, namely ICG.

This deal included Architel's flagship product ASAP as well as two acquired products from Accugraph, namely Objectel and OMS. Architel's stated strategy has been to grow through acquisition and without doubt this transaction enabled the company to change the competitive landscape enabling us to expand our product portfolio, strengthen our sales, engineering, professional services and engineering groups and significantly expand our customer base.

LAUNCH OF "BEST-IN-SUITE" PRODUCT STRATEGY

With the completion of the acquisition of Accugraph as well as the development of a new product to address the OSS Interconnection market, known as InterGate, we transitioned the company to support four product lines and launched our "Best-in-Suite" strategy. This concept is designed to help new customers, in particular CLECS and start-ups, reduce the risk, cost and effort of delivery by procuring a suite of integrated products from a single vendor. This strategy has been successfully presented to many customers around the world and has, without exception, been universally endorsed. However, the "Best-in-Suite" concept also provides our customers the flexibility to install "a product at a time" which is more relevant in established telecommunications service providers. This strategy provides Architel with a significant competitive advantage over other OSS vendors by being able to meet the needs of all types of service providers in a flexible and dynamic manner.

to our shareholders

SUCCESS IN EUROPE

Over a year ago, we announced that we would make a major investment in the European marketplace. Our investment has provided an outstanding return with European revenues growing from 1% of total revenue in 1997 to 29.4 % in 1998. This has been enabled by leveraging our strategic partners in the European market with very effective support from our direct sales team based out of London, England. We successfully closed license agreements in partnership with Ericsson at Telecom Eireann and KPN Telecom in the Netherlands, with Andersen Consulting at AirTel in Spain and Cable and Wireless in the United Kingdom and with AMS at Mannesmann Arcor in Germany.

Clearly, these were all major wins in a highly competitive environment that not only proved our product superiority, but entrenched our strategic relationships with key partners and significantly enhanced our European profile. Given the lack of an entrenched OSS vendor in the European marketplace we believe we are positioned stronger than ever to capitalize on this success. We have now established a strong European base of over 25 employees with sales coverage across Europe, the Middle East and Africa and are very well positioned to take further advantage of European deregulation over the next year

EXPANSION OF OPERATIONAL CAPABILITY

During 1998 we increased our employee base from 211 employees to 414 employees and expanded our infrastructure in Toronto, Dallas and the United Kingdom. We established a dedicated channel sales group to support our strategic partners, significantly expanded direct sales coverage across Canada, the United States and Europe and more than doubled the capacity of our Professional Services organization. With the consolidation of the Accugraph and Architel Engineering groups into Architel's head office in Toronto we established a truly world-class engineering group highly focused on continuing to develop and evolve our product solutions. With the completion of the acquisition and through new hires we also further strengthened our senior management team. As a customer focused organization we will continue to make the necessary investments to meet our customer's demands in 1999.

OUTSTANDING FINANCIAL PERFORMANCE

Our financial performance in 1998 was exceptional. Total revenues for the year were $50.8 million, an increase of 54% over revenues in the previous year. This included a fourth quarter of $18.7 million, an 88% increase over the comparable quarter last year and 62% higher than the third quarter. On a fully diluted basis, earnings per share before amortization of intangibles was $0.56, up 75% from the previous year. We completed the fiscal year with cash and negotiable securities of $31 million. Our strong financial performance differentiated us from our competitors and provided our customers with confidence in an industry characterised by under-performing OSS software vendors.

NEW CUSTOMERS

The ultimate success of any software company is measured by the customers who use its products. The facts speak for themselves. As a merged company we have sold our products to over 40 communications providers around the world. During this fiscal year we successfully penetrated the growing CLEC market in the United States and Canada with the addition of various high profile CLECs including MetroNet, Sprint Canada, Teligent and ICG Communications. We established ourselves as a leader in Europe and won our first contract in Latin America with Avantel of Mexico. We continue to be able to provide solutions to all types of telecommunications service providers as a result of our focus on providing flexible, open, scaleable, product offerings that can support multiple service offerings across multi-vendor networks. We will continue to dedicate ourselves to earning our customers' business and delivering solutions that meet their needs.

1998 was an incredible year that exceeded even our expectations. We transformed the company into the OSS leader in the provisioning marketplace. We have a sound product strategy backed by an enthusiastic, dynamic and highly motivated workforce that is ready to deliver innovative, reliable and robust product solutions to customers around the world. We have a seasoned senior management team. Our fundamentals are sound. We are operating in a rapidly growing, dynamic industry that continues to display strong demand for our products and services. All of these factors give us a competitive advantage and strong platform from which to grow. We thank our employees for their dedication, commitment and enthusiasm and our customers, shareholders, strategic partners and suppliers for their support. We embark upon the final year before the millennium with enthusiasm and confidence and a total focus on being the OSS software provider of choice to the global telecommunications industry.

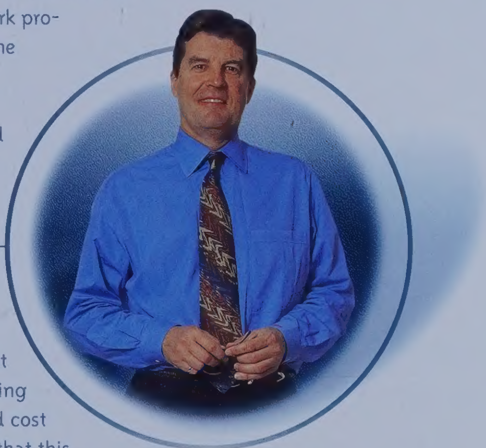
ANTHONY P. VAN MARKEN
President and Chief Executive Officer

the new frontier

When we founded Architel in 1984 it was with a mission to add value and create products that telephone companies could use. A decade and a half later, we have evolved as a leading supplier of Operations Support Systems to the global telecommunications marketplace and are viewed as the leading provider of software products that address the total provisioning needs of all types of communications providers, wherever they may be in the world. During this same period of time, the telecommunications landscape has been dramatically altered through legislation, de-regulation, technological innovation and competition. As a result, we have also refined our strategy, our focus and our plans. As Tony van Marken has discussed our performance, I will share with you our vision for the future.

Service Delivery is one of the key challenges facing service providers, irrespective of the type of service to be provided. The battle for market share will not just be based on marketing and technology. The ability of service providers to truly differentiate themselves will be based on how they deliver service to customers. The ability to do this depends directly on the back office infrastructure and therefore on the quality of the Operations Support Systems they have deployed. In addition, to achieve truly outstanding performance the front office and back office need to be integrated in a transparent manner. This has been further complicated by legislation such as the Telecom Reform Act which mandates that the OSS infrastructure of service providers must communicate with each other in a secure, reliable manner to facilitate wholesale/retail business models.

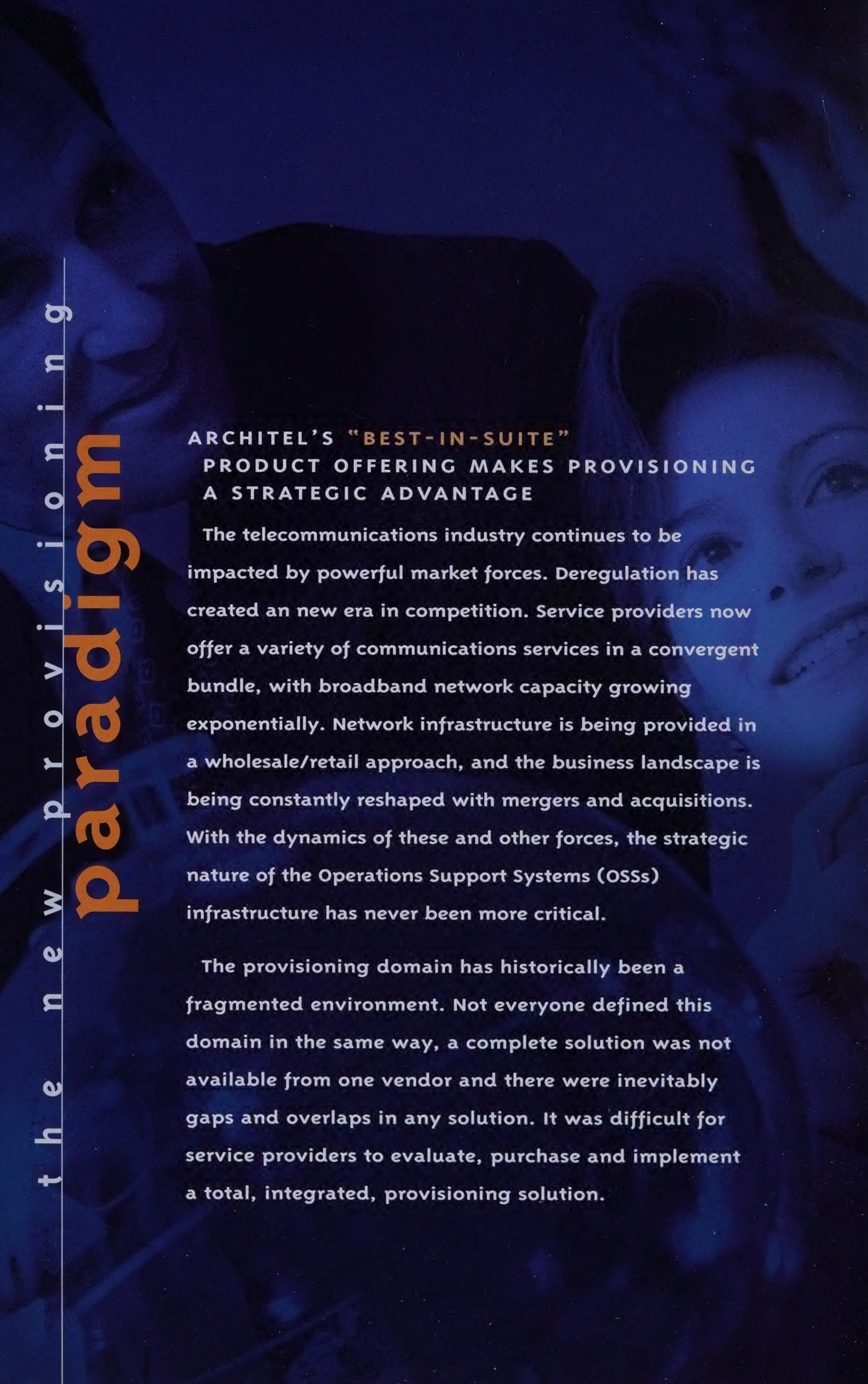
These challenges are non-trivial, but are precisely the focus of Architel's product strategy which is aimed at providing integrated solutions that enable telecommunications service providers to provision any type of service across any type of network with speed and efficiency and at the lowest cost. We established our leadership position in the telecommunications industry by being the first vendor to provide a convergent service activation platform that could activate voice and data services across heterogeneous networks. This product, known as ASAP, was released in 1992 and is now the leader in its product category with more installations than any other competitor. However, as we enjoyed the success of ASAP, our flagship product, we recognized the need to address the end-to-end provisioning needs of service providers. In 1997 we started the development of an Order Management product and followed this up in 1998 by initiating a project to build an OSS InterConnection Gateway. Realizing this was not enough, we acquired Accugraph, consolidated our joint product efforts, and provided a vision for the industry of a suite of products that could be deployed to address the challenge of service and network provisioning, from the receipt of the service order to the delivery of service to the customer, while ensuring the co-ordination and tracking of all manual and automated tasks associated with the provisioning process.



Today, we call this "Best-in-Suite", a concept based on the premise of taking "Best-in-Class" product components and pre-integrating them to reduce risk, effort and cost of delivery. We are confident that this strategy will provide a sound platform from which to grow the company.

Our mission is to make our OSS solutions indispensable to the telecommunications service providers of the world. This is a formidable challenge and one that we are meeting head on. However, it goes beyond where we are today as a company. It means continually improving our performance, refining and simplifying our products and never ceasing in our quest to make our customers successful. It means hiring and retaining the very best employees, giving them an environment in which to excel and the self-confidence to make decisions and take action. It also means, developing new products organically and acquiring new assets that are synergistic to our existing product offerings. Ultimately, our goal is to provide as much value as possible through a singe source — Architel. Our strategy is clear. Our mission achievable. We are looking forward to the 21st Century.

DAVID E. CURRY
Co-founder and Senior Vice President, Business Development



the new provisioning paradigm

ARCHITEL'S "BEST-IN-SUITE" PRODUCT OFFERING MAKES PROVISIONING A STRATEGIC ADVANTAGE

The telecommunications industry continues to be impacted by powerful market forces. Deregulation has created an new era in competition. Service providers now offer a variety of communications services in a convergent bundle, with broadband network capacity growing exponentially. Network infrastructure is being provided in a wholesale/retail approach, and the business landscape is being constantly reshaped with mergers and acquisitions. With the dynamics of these and other forces, the strategic nature of the Operations Support Systems (OSSs) infrastructure has never been more critical.

The provisioning domain has historically been a fragmented environment. Not everyone defined this domain in the same way, a complete solution was not available from one vendor and there were inevitably gaps and overlaps in any solution. It was difficult for service providers to evaluate, purchase and implement a total, integrated, provisioning solution.

During 1998, Architel forever changed the way that provisioning systems are viewed by the telecommunications industry. With the "Best-in-Suite" strategy, we now offer the first complete provisioning suite, based upon superior, best-in-class products. This new paradigm creates significant advantages for Architel and our clients by allowing "one-stop" shopping for a complete provisioning solution with a great deal of flexibility for a variety of implementation strategies. With an integrated, "Best-in-Suite" solution, provisioning becomes a strategic advantage for service providers, and can form the cornerstone of a complete service-fulfillment solution.

HOW CAN SERVICE PROVIDERS STAND OUT?

As competition in the telecommunications industry continues to intensify service providers are challenged to attract and retain valuable customers in order to be successful. To differentiate themselves, service providers must offer more services and provide better customer service while reducing cost. Architels' provisioning suite is uniquely positioned to provide these business benefits.

Our products are designed to support the flexible bundling of a variety of service offerings. The service definitions are controlled by business rules, which are abstracted from the underlying technology. With Architel's technology, a service provider can change service offerings, or the way services are provided, without the need for costly software development. Outstanding customer service is provided instantly and with accurate information. Based on a flow-through provisioning paradigm, Architel's fully integrated solution provides instant access to inventory information, management of service order processing and coordinated, real-time command of all network elements.

To be a low-cost service provider, Operations Support Systems must support complete and efficient flow-through. The advantages are that the service provider can meet competition on the most favorable terms. Architel's systems are designed to eliminate or reduce operating costs by the nature of coordinated, flow-through business processing. By building layers of independence and technical insulation in our products, on-going changes and enhancements in the business process can be implemented quickly in the provisioning system without costly "ripple effects".

In addition to these fundamental provisioning system advantages, service providers can standout by implementing the solution quicker and with less risk than their competition. Architel's provisioning suite provides a complete solution from a single vendor. The cost and risk of integrating multiple third party products is eliminated with this "Best-in-Suite" approach. In addition, service providers can work with Architel and our strategic partners to implement our solution ensuring world-class delivery in a timely manner.

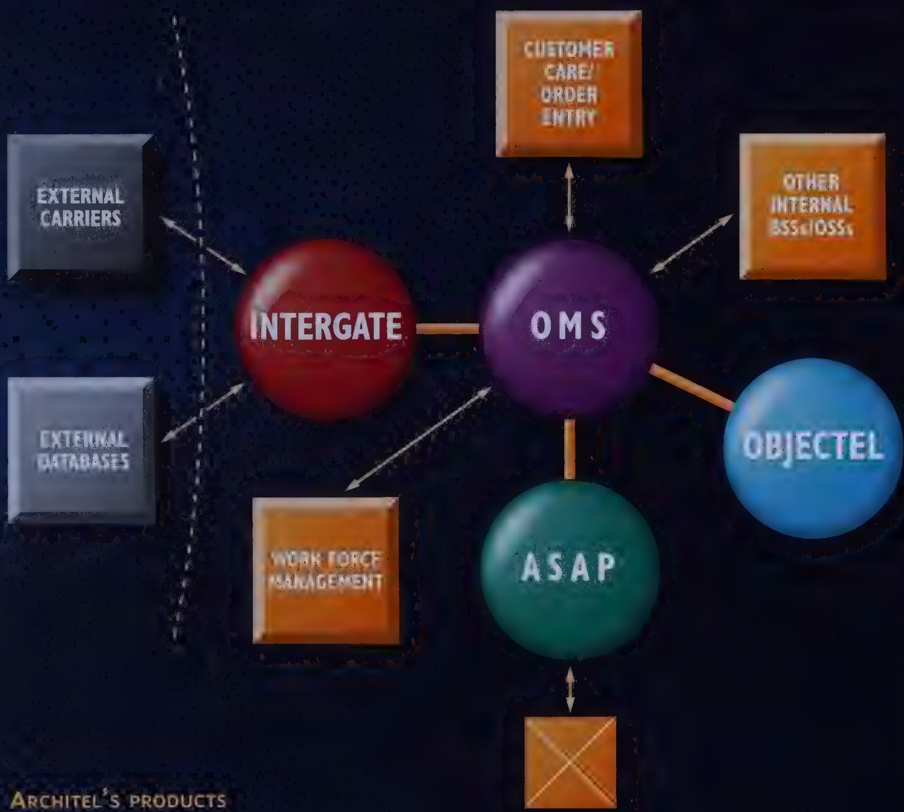
the complete

architel's "best-in-suite"

provisioning

Provisioning is a major component in the service provider's fulfillment process. The Architel provisioning suite provides a complete and accurate inventory of all network capacity. It interacts with the service ordering process and instantly determines the network capacity available for sale. These systems design and assign network facilities for the requested service and command all required network elements in a flow-through, timely manner. Throughout this process, the provisioning suite coordinates the many tasks involved in fulfilling the complete service order, which often involve several other support systems and staff. Additionally, service providers often resell certain services or partner with other companies for portions of the complete service offering. In these cases, certain tasks of the service order are communicated through gateways and fulfilled by trading partners.

provisioning solution



ARCHITEL'S PRODUCTS ARE ALL BUILT TO DEMANDING TECHNICAL SPECIFICATIONS. THEY PROVIDE A HIGH DEGREE OF FLEXIBILITY USING TECHNIQUES FOR ABSTRACTING THE BUSINESS PROCESS FROM THE UNDERLYING TECHNOLOGY.

All products support convergent services in the wireline, wireless, transport and broadband network domains. These products use multiple insulation layers to manage the effects of business process change and independence layers to isolate 3rd party components. The proven scalability of our products allows the system to support start-up service providers, large regional service providers and PTTs. As mission-critical systems, they support a wide variety of interfaces ranging from contemporary, standards-based methods to traditional approaches, commonly found in most telecommunications networks.

architel's "best-in-suite" offering is made up of
four key products

OMS

Architel's Order Management System (OMS) provides control and co-ordination of the provisioning lifecycle of a telecommunications service order.

The workflow of both manual and automated tasks may be managed by OMS. Manual tasks may be automated using metrics and tools of the OMS system, with a priority and pace determined to best fit the unique conditions of that service provider. Flexible interface tools allow OMS to work with many internal and external support systems to provide complete, flow-through automation of an integrated environment. OMS provides complete logging and audit trails for full control of the provisioning process. A powerful user GUI supports the definition of business rules, as well as, management of individual worklists. With OMS, the service provider realizes standardization of the service delivery process, integration and automation for rapid service delivery and a full-function platform for continuous process improvement.

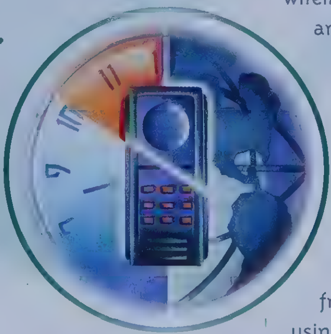
OBJECTEL

The Objectel product enables total inventory management for facilities - based service providers, with integrated functions ranging from network engineering to service design and assignment of network resources.

As a third-generation inventory product, Objectel provides network models and specific functionality for a wide variety of network domains including SONET/SDH, ATM, Frame Relay, IP, and most circuit-based technologies. It provides both physical and logical inventory functions, which serve a range of constituents in the service provider staff. With Objectel, service providers can completely manage their network capacity, identify and allocate network resources for specific customer needs, and forecast growth requirements for a variety of network elements.

ASAP

Automatic Service Activation Program (ASAP), in its fourth generation, enables the convergent activation of voice and data services in multi-vendor networks.



ASAP provides coordination and control of the commands to activate network elements across any type of technology domain including wireline, wireless, data, broadband and customer-premise equipment. ASAP abstracts the service definition from the technical language of a multitude of network elements. With ASAP, a truly convergent service provider may activate a bundled service offering from a single service order, using high-level service commands. Using this approach, the service provider may add or change the support of the network elements, without the need for costly system programming. ASAP provides instant activation and real-time confirmation of any type of service offering across any type of network technology.

INTERGATE

Architel's InterGate, our most recent product offering, brings our technical superiority and experience to the domain of OSS inter-connection between service providers and their trading partners.

This product provides an automated and secure interconnection gateway for any type of transaction such as pre-ordering, ordering and post-order completion. Transactions may be standards-based or may use a proprietary format. With InterGate, the service provider may automate all aspects of the interactions with multiple trading partners such as between wholesalers and retailers, subscriber networks and transport networks, network trouble reports, unbundled loop requests, and so forth. Being integrated with the provisioning suite, the service provider can manage the entire provisioning process, even when some portions are performed by other companies.

the ultimate competitive weapon

Architel's provisioning suite builds upon the strengths of each best-in-class product with the result being an offering that is "Best-in-Suite". With superior technology, proven scaleable performance and business process flexibility, Architel's provisioning suite is setting the standard for systems in today's competitive market. Integrated for flow-through, interactive processing, the suite provides a complete provisioning solution from a single vendor with a record of delivery in the industry. Once implemented Architel's suite provides the competitive weapon service providers require in order to successfully deliver service and differentiate themselves from their competitors.

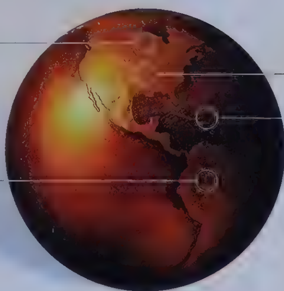
architel customers

canada

- BC TEL
- Bell Mobility
- Manitoba Tel
- MetroNet
- Microcell
- MT&T
- NBTel
- NewTel Communications
- Rogers Cablesystems
- Rogers Cantel
- Sprint Canada

united states

- Ameritech
- Bell Atlantic[1]
- Cable and Wireless (US)
- GTE
- ICG Communications
- MCI WorldCom[2]
- MindSpring
- Teligent
- U S WEST
- VarTec

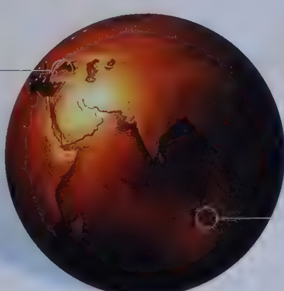


latin/south america

- Amaritel (Mexico)
- Avantel (Mexico)
- Embratel (Brazil)

caribbean

- Bermuda Telephone
- Cable and Wireless Jamaica



europe

- AirTel (Spain)
- British Telecom (UK)
- Cable and Wireless Communications (UK)
- Energis Communications (UK)
- Infostrada (Italy)
- KPN Telecom (Netherlands)
- Mannesmann Arcor (Germany)
- TeleNor (Norway)
- Telecom Eireann (Ireland)

asia/pacific

- COINS (Malaysia)
- Telecom New Zealand
- TIME Telekom (Malaysia)

Note: (1) Bell Atlantic, an ASAP licensee, merged with NYNEX, an ASAP licensee during 1997. The surviving company entity is indicated only.

Note: (2) WorldCom, an ASAP licensee acquired MCI, an ASAP licensee during 1997. The surviving company entity is indicated only.

OVERVIEW

The Company derives substantially all of its revenue from licensing Operations Support Systems (OSSs) to telecommunication service providers and providing related services. Until mid-1998, revenues were predominately attributed to the Company's service activation software product, Automatic Service Activation Program (ASAP), with a relatively small percentage of revenues attributed to the Company's work force management product, Field Access Management Information System (FAMIS). On June 29, 1998, the Company acquired Accugraph Corporation in a share exchange transaction. As a result, the Company now markets and sells an integrated suite of provisioning solutions, which includes ASAP (a service activation system), Objectel (an inventory, assignment and design system), OMS (an order management system) and an interconnection gateway product currently under development (a system allowing for electronic communication between telecommunications service providers). The results of operations of Accugraph have been combined with those of the Company since the date of acquisition (see Note 12 to the Notes to the Consolidated Financial Statements).

Earnings in fiscal 1998 were affected by the Accugraph acquisition, which was accounted for using the purchase method. The total value of intangibles acquired was $37.9 million, which will be amortized over a period ending in the third quarter of fiscal 2000, with $5.6 million being amortized in fiscal 1998. During fiscal 1997 and 1996, earnings were affected by the amortization of a $3.0 million payment made to a third party in lieu of a pre-existing royalty obligation in respect of ASAP licenses. The following chart shows revenues, net income and fully diluted earnings per share, and net income and earnings per share excluding the effect of amortization of intangibles/royalties, for the past three fiscal years.

	Years ended September 30		
	1998	1997	1996
Revenue	**$ 50,775,182**	$ 33,034,436	$ 17,976,168
Net income for the year	**2,320,776**	4,225,847	2,192,222
Fully diluted EPS	**0.17**	0.32	0.20
Net income for the year excluding the effect of amortization of intangibles/royalties	**7,941,145**	5,369,642	2,761,080
Fully diluted EPS excluding the effect of amortization of intangibles/royalties	**0.56**	0.41	0.24

In recent years, the Company has earned the majority of its revenues from sales denominated in U.S. dollars, while most expenses have been incurred in Canadian dollars. Accordingly, the Company's operating results have been, and will continue to be, affected by changes in the exchange rate between the U.S. and Canadian currencies and, to a lesser extent more recently, changes in the exchange rate between the UK and Canadian currencies. Specifically, an appreciation of the Canadian dollar in comparison to the U.S. dollar or the U.K. pound could adversely affect results. As the Company continues to expand its operations internationally, it will be exposed to currency fluctuation risks with respect to other foreign currencies. Changes in exchange rates relative to the Canadian dollar will continue to have a material impact on the Company's future operating results, as it is anticipated that the significant majority of the Company's revenues will be from sales denominated in currencies other than the Canadian dollar. Historically, the Company has not engaged in hedging its foreign currency-denominated sales, and will continue to assess the advisability of doing so.

The following discussion relates to the Company's results as reported in Canadian dollars and under Canadian generally accepted accounting principles. See note 14 of the Notes to the Consolidated Company's results under the United States generally accepted accounting principles compared to Canadian generally accepted accounting principles.

RESULTS OF OPERATIONS

The table below sets forth, as a percentage of total revenues, items from the Company's Consolidated Statement of Operations for the fiscal years ended September 30 indicated:

	1998	1997	1996
Revenue:			
License fees	**52.0%**	63.2%	69.3%
Services and other	**48.0**	36.8	30.7
Total revenue	**100**	100	100
Cost of sales			
License fees	**1.1**	–	–
Services and other	**28.9**	25.6	23.5
	30.0	25.6	23.5
Gross profit	**70.0**	74.4	76.5
Operating expenses			
General and administrative	**11.2**	14.3	19.9
Sales and marketing	**17.2**	16.6	12.3
Research and development	**19.3**	21.2	21.6
Royalties	**–**	6.0	6.8
Total operating expenses	**47.7**	58.1	60.6
Income from operations	**22.3**	16.3	15.9
Interest income	**3.9**	5.4	5.5
Amortization of intangibles	**(11.1)**	–	–
Income before income taxes	**15.1**	21.7	21.4
Income taxes	**10.5**	8.8	9.2
Net income	**4.6**	12.9	12.2

REVENUE

In thousands	1998	1997	1996
License fees	**$ 26,407**	$ 20,890	$ 12,455
Percentage increase over prior year	**26%**	68%	96%
Services and other	**24,368**	12,144	5,521
Percentage increase over prior year	**101%**	120%	15%
Total	**$ 50,775**	$ 33,034	$ 17,976
Percentage increase over prior year	**54%**	84%	61%

A typical sale involves the licensing of the Company's software product(s) together with the provision of professional services (consulting, installation, implementation, customization and training) and post implementation support and maintenance of the licensed software or total solution. Frequently, the Company will enter into an interim arrangement with a prospective customer pending execution of a final agreement in order to commence work on an implementation project. In such cases, the Company will earn professional services revenue and a license rental fee.

License fees are determined based on a number of factors related to the scope of use of the software, such as the telecommunication services, size of network and geography supported by the software. Most transactions involve a one-time up-front license fee or an up-front fee with additional one-time fees based on the growth of the customer's operations and use of the Company's software. Occasionally, an alternative pricing option, designed to address the financial needs of start-up companies, is used, which provides for a lower initial fee, with ongoing periodic license fee payments based on the use of the Company's software. This pricing alternative provides the Company with the potential for recurring license fees that grow as the customer's use of the Company's software grows. At the same time, it results in lower license fee revenues in the short term and exposes the Company to risk that such on-going license fees will not be realized due to the customer's business failing to succeed or grow, the customer ceasing use of the Company's software or the customer failing to remain solvent.

Professional services are provided to complement a product license. Such services are most often provided on a time and materials basis and occasionally on a fixed price basis. Often, the Company is retained as subcontractor to a systems integrator retained to implement the Company's product, although on occasion, the Company has acted as prime contractor. Professional services may be provided at a customer site following initial implementation, depending on the needs of the customer, with the result that professional services may continue to be earned after the corresponding license fee revenue has been recognized.

Software support fees, usually payable annually in advance, generally range from 15% to 22.5% of the license fee per annum and are recognized over the period of the support contract. Revenue from software support generally commences upon first production use of the software. Software support includes problem fixes as well as certain upgrades to the licensed software.

The Company has traditionally derived a majority of its revenues from license fees, although, in recent years, services revenue has grown as a percentage of revenues. This is due to a number of factors principally related to the Company's increased focus on the new telecommunications service providers, especially in North America. This has resulted in revenues being derived from a larger number of customers, including some where, due to the relatively smaller size of the customer, the license fee represents a smaller percentage of the overall revenue from the project. This was especially the case where the alternative pricing option described above was utilized. Recently, the Company has experienced a number of situations where customers preferred to contract directly with the Company to provide the required implementation services, rather than employing a larger systems integrator, resulting in a larger scope of professional service work than had been experienced previously. Similarly, as part of a general outsourcing trend in the industry, certain customers desire to retain the Company for post implementation solution support. Finally, on-going product support revenues continue to grow, as the Company's customer base expands. As a result, it is expected that the percentage of revenues represented by services will continue to increase and may represent the majority of revenues in future periods. Offsetting this trend are license fees derived from certain application software that the Company has previously provided on a service fee basis and license fee revenue derived through the Company's sales channel partners, especially in those geographies where the Company does not intend to establish a large professional services group at this time, such as Latin and South America and Asia/Pacific.

The usage-based pricing option described above is designed to provide more recurring license fee revenue for the Company, but is not expected to have a material impact on revenues in the short term. To date, it has been chosen by only a few customers. Following the acquisition of Accugraph, the Company was successful in selling some of the new software products to existing customers and the Company believes that further cross selling opportunities exist. There also exists the opportunity to obtain additional license fees from existing clients, based on expanding the scope of a license previously granted; however, the Company continues to rely primarily on sales to new customers to generate additional license fee revenue. While the majority of the Company's revenues are still being derived from large contracts with a relatively small number of customers, customer concentration has lessened. During fiscal 1998, no one end-user customer accounted for more than 10% of revenues and slightly in excess of 50% of revenues was attributed to 7 end-user customers, compared to 69% of revenue being attributed to 3 end-user customers during fiscal 1997. Revenue attributed to sales channel partners increased significantly in fiscal 1998, growing to 31.4% of total revenues from less than 1% in fiscal 1997, with revenue attributed to sales effected

through Ericsson accounting for 18.8% of revenues in fiscal 1998. Sales cycles continue to be lengthy, especially with the larger telecommunications service providers and increasing competition in the start-up market is sustaining pricing pressures. Accordingly, the potential for quarterly revenue fluctuations is expected to continue, at least in the short term.

LICENSE FEES

During fiscal 1998, license fee revenue was derived from a total of 17 customers, 13 of whom licensed ASAP, 2 of whom licensed Objectel, 1 of whom licensed OMS, and 1 of whom licensed the suite of ASAP, Objectel and OMS. The majority of the license fee revenue in fiscal 1998 was derived from 5 customers, which included one customer (a large independent telecommunications service provider in the United States) for whom the related project commenced during fiscal 1997 but was mostly completed in 1998, and four new customers (two PTT's and a start-up provider in Europe, and a Competitive Local Exchange Carrier (CLEC) in the United States). Opportunities in the North American market were impacted by large incumbent carrier focus on Year 2000 issues and resultant delays in procurement of new non-Year 2000 impacted systems. Accordingly, new license opportunities in North America were primarily in the new entrant or CLEC market. It is expected that Year 2000 issues will decline in importance for the larger carriers near the end of 1999, although it is uncertain as to how this will impact new system procurement. In Europe, opportunities continue to be present at both the incumbent carriers (PTT's) and the new entrants. In one instance, Year 2000 issues prompted the selection of the ASAP product.

In fiscal 1997, license fee revenue was derived from a total of 10 ASAP customers, 5 of which commenced projects in prior years. License fee revenue was higher in fiscal 1997 than in fiscal 1996, principally due to a higher number of larger customers with higher license fees. The majority of the license fee revenue in fiscal 1997 was derived from 5 customers, which included two customers (one RBOC and one Competitive Access Provider) for whom projects commenced during fiscal 1996 but were mostly completed in 1997, and three new customers (an RBOC, a large independent telecommunications service provider, and a Competitive Access Provider).

In fiscal 1996, license fee revenues were derived from a total of 9 customers, 4 of which commenced projects in the prior year. These license fee revenues were principally derived from new ASAP licenses to 2 RBOCs, a Competitive Access Provider and a wireless provider.

The Company does not actively sell its work force management product and therefore did not generate material license fee revenue from it during fiscal 1998, 1997 or fiscal 1996. Similarly, while the Company continues to support certain legacy products acquired in the Accugraph acquisition, it has not generated material license fee revenue from such products.

SERVICES AND OTHER

Services and other revenue consist of professional services (which includes training), product support and commissions earned on required third party software. Professional services revenue is generally recognized on a time and materials basis and varies between contracts depending on the level of the Company's involvement in the implementation of the Company's software.

Professional services revenue in fiscal 1998 totaled $18.4 million compared to $9.1 million in fiscal 1997 and $3.7 million in fiscal 1996. In fiscal 1998, professional services revenue was earned at 31 customer or partner accounts, with over 70% of such revenue attributed to 9 customers. In fiscal 1997, professional services revenue was earned at 18 customer or partner accounts, with over 70% of such revenue attributed to 3 customers. The increase in professional services revenue in fiscal 1998 was due to larger implementation projects for a larger number of customers.

Product support revenue in fiscal 1998 totaled $5.8 million (11% of revenues) compared to $3.0 million (9% of revenues) in fiscal 1997 and $1.5 million (8% of revenues) in fiscal 1996. Support revenues were generated from 21 Architel customers during fiscal 1998 (16 related to ASAP and 5 related to FAMIS/Handheld products) and numerous customers from Accugraph's legacy customer base. This compares to 15 support customers during fiscal 1997, of which 10 related to ASAP and 5 related to FAMIS/Handheld products. Product support revenues are expected to continue to grow as new licenses are sold.

Also included in services and other revenue is commission earned on third party software licensed by the Company's customers in conjunction with the license of ASAP, although such commissions are relatively insignificant. Commencing in mid 1998, the Company began relicensing such third party software, revenues from which are included in license fees and the cost of which is reflected in cost of sales.

SALES BY GEOGRAPHIC REGION — ALL CATEGORIES COMBINED

In thousands	**1998**		1997		1996	
Canada	**$ 6,330**	**12.5%**	$ 2,233	6.8%	$ 2,737	15.2%
United States and Caribbean	**28,604**	**56.3%**	29,333	88.8%	11,819	65.8%
Europe	**14,929**	**29.4%**	877	2.6%	256	2.0%
Asia Pacific	**912**	**1.8%**	591	1.8%	3,064	17.0%
Total	**$ 50,775**	**100%**	$ 33,034	100%	$ 17,976	100%

Over the past three years, the significant majority of the Company's sales have been made to customers located outside of Canada. The high percentage of sales in the United States over the last three years reflects the Company's focus on this market to take advantage of demand for provisioning solutions as a result of competitive pressures created by telecom reform in 1996. Sales efforts in the United States during fiscal 1998 were primarily focussed at CLEC's, as fewer opportunities were identified within the RBOC market, due to mergers and RBOC focus on Year 2000 issues. The Company expects that demand for its provisioning solutions will remain strong in the United States over the foreseeable future. Since the telecom market deregulation of Europe on January 1, 1998, the Company has expanded its efforts in this market, with a marked increase in the revenue derived from this market. The Company expects that the percentage of its revenues derived from the European Community will increase in fiscal 1999 and subsequent years. The Company delayed focussing sales efforts in the Asia/Pacific region during fiscal 1998, as a result of economic factors negatively affecting this market and greater opportunities elsewhere in the world. During fiscal 1999, the Company intends to start to make sales investments in this region with a view to achieving greater penetration of this market, primarily through sales channel partners.

EXPENSES

Cost of Sales

In thousands	**1998**	1997	1996
Cost of license fees	**$ 575**	$ –	$ –
Cost of services	**14,650**	8,472	4,237
Percentage increase in costs of services over prior year	**73%**	100%	49%

Cost of license fees consists of the cost of third party software embedded in the ASAP product, which is resold by the Company as part of an end-user license. The associated revenues are included in license fee revenues.

Cost of services consist mainly of personnel, direct and related overhead costs associated with providing professional services and product support. Margins on services revenue (excluding third party commissions) increased to 39.4% in fiscal 1998 from 30.0% in fiscal 1997, and from 18.5% in fiscal 1996. Margins on services increased in fiscal 1998 due to increased margins on professional services, including training, and on product support and on achievement of bonus milestones on a professional services project. Margins on services increased in fiscal 1997 due to increased margins within the product support group, resulting from additional support customers, and was partially offset by a small decline in the professional services margin due to a significant increase in the size of this organization during the year. Margins on services may decline in fiscal 1999, due to low margins on certain fixed price contracts assumed on the acquisition of Accugraph, low margin third party subcontracted services engaged by the Company on a project throughout the year and further investments being made in the managerial level of the professional services organization to support increased project activity.

Gross profit, as a percentage of total revenues, declined in fiscal 1998 compared to fiscal 1997, and in fiscal 1997 compared to fiscal 1996. This decline in gross profit margin was due to services revenue making up a larger portion of total revenues and in fiscal 1998 was also attributed to low margins on relicensed third party software embedded in the ASAP software and on third party subcontracted services work at a customer. The decline in the gross profit margin is expected to continue, at least in the short term, as the trend toward professional services representing a larger percentage of total revenues continues and margins on such activities decline, for the reasons described above.

GENERAL AND ADMINISTRATIVE

In thousands	**1998**	1997	1996
General and administrative expenses	**$ 5,708**	$ 4,732	$ 3,570
Percentage increase over prior year	**21%**	33%	115%

General and administrative expenses consist primarily of salaries and benefits of all executive, administrative, human resource, finance, legal and internal information technology service personnel. General and administrative expenses also include adjustments reflecting foreign exchange translations. While such an adjustment was not significant in fiscal 1996, a favorable adjustment of approximately $1,100,000 was realized in fiscal 1998, compared to $100,000 in fiscal 1997, as a result of the decline in the Canadian currency exchange rate relative to the U.S. dollar during that period.

As a percentage of revenue, general and administrative expenses fell to 11.2% in fiscal 1998 (13.4% before foreign exchange gains) from 14.3% in fiscal 1997 (14.6% before foreign exchange gains), and 19.9% in fiscal 1996, as the Company was able to absorb these costs over a broader revenue base. Included in general and administrative expenses for fiscal 1998 was a bad debt allowance of $631,000, relating to a receivable from a customer in Malaysia.

During fiscal 1998, further head office expansion in Toronto occurred to accommodate the combined Toronto operations of the Company and Accugraph, as well as to accommodate anticipated growth. The head office facilities in Toronto support all administrative functions including finance, human resources, legal and information technology services. During fiscal 1997, the Company opened a UK office in London, England to support its European sales and services activities. In addition, late in fiscal 1997, an office was opened in Dallas, Texas to support regional sales and services groups and the Company's industry marketing group. Future increases in general and administrative expenses will be dependent upon the level of administrative resources required to support additional revenue from license fees and services. With respect to office facilities, a further head office expansion of approximately 13,500 square feet in Toronto commenced in January 1999 and future additional European and new Asia/Pacific facilities may occur depending on growth opportunities in these regions. Nevertheless, it is expected that, in the short term, general and administrative expenses will continue to decline slightly as a percentage of revenues.

SALES AND MARKETING

In thousands	**1998**	1997	1996
Sales and marketing expenses	**$ 8,713**	$ 5,488	$ 2,208
Percentage increase over prior year	**59%**	149%	63%

Sales and marketing expenses include salaries, benefits and commissions paid to sales, product and industry marketing, and channels personnel, and expenses related to trade shows, conferences, promotional activities, marketing communications materials, travel and other overhead costs. Sales and marketing expenses increased in 1998 principally as a result of the expansion of the sales personnel and related infrastructure, particularly in the channels and sales support organizations, both as a result of internal growth and the acquisition of Accugraph. It is expected that sales and marketing expenses will continue to grow as a percentage of revenues for the 1999 fiscal year, as the Company focuses on maintaining its revenue growth.

RESEARCH AND DEVELOPMENT

In thousands	**1998**	1997	1996
Research and development	**$ 9,823**	$ 6,989	$ 3,876
Percentage increase over prior year	**41%**	80%	279%

Research and development expenses consist primarily of technical research and development personnel salaries and benefits, consulting fees, equipment leases, travel expenses and other attributable overhead costs. In accordance with generally accepted accounting principles in Canada, the Company has expensed all research costs as incurred. Development costs have also been expensed as they have not met the criteria for deferral under generally accepted accounting principles.

Research and development costs increased significantly in fiscal 1998, fiscal 1997 and fiscal 1996, but declined slightly as a percentage of revenues. Expenses during fiscal 1998 related to further product enhancements for existing products, new product development, development of certain reusable implementation applications normally developed for customers on a time and materials basis, and further investments in testing and other internal capabilities. For the foreseeable future, the Company intends to maintain a level of research and development expenditures, as a percentage of revenues, at least equal to that for fiscal 1998 for continued new product development, reusable implementation application development, enhancements to existing products and product suite integration.

Under the Income Tax Act (Canada), certain research and development activities performed by the Company qualify for investment tax credits which accrue at a rate of 20% of eligible research and development expenditures. These credits are recorded when there is reasonable assurance of realization and, accordingly, the Company accrues a portion only of the total credits claimed. Such accruals are netted against gross research and development expenses. To the extent that the actual credit realized exceeds or is less than the accrual, the difference will be realized in the period when such difference is determined. See note 14 to the Notes to the Consolidated Financial Statements.

ROYALTIES

In thousands	**1998**	1997	1996
Paid to NBTel	**$ –**	$ 75	$ 231
Amortization of royalty	**–**	1,913	997
Total royalty expenses	**$ –**	$ 1,988	$ 1,228

Cash royalties and amortization of royalty relate solely to a prior arrangement with NBTel (New Brunswick Telephone Company Limited). Under an agreement with NBTel, the Company was obligated to pay royalties to NBTel at a rate of 20% for ASAP sales in Canada and 15% elsewhere. In fiscal 1996, the Company paid $3.0 million to NBTel in lieu of all future royalties, as further described in note 5 to the Consolidated Financial Statements. This $3.0 million payment was amortized against income based on ASAP license fee revenue. The increase in royalties in fiscal 1996 and fiscal 1997 was principally as a result of increased sales of ASAP licenses. The amortization of the $3.0 million payment was completed in the fourth quarter of fiscal 1997. In addition, no further cash royalties remain to be paid.

INTEREST INCOME

The large increase in interest income in fiscal 1997 and fiscal 1996 was principally a result of the investment of the proceeds from the Company's initial public offering in March 1996. The increase in interest income in fiscal 1998 was due to the additional investment of cash from operations, although at prevailing markets rates below that of the remainder of the investment portfolio. It is anticipated that the current levels of interest income will continue for the near future, unless adverse interest rate fluctuations occur in the fixed income market, as positive cash flows from operations are expected.

INCOME TAXES

	1998	1997	1996
Income tax rate	**68.4%**	40.8%	42.9%

The Company's combined Canadian statutory income tax rate currently approximates 44.6% and the actual effective tax rate can vary from the statutory rate due to income being earned in foreign jurisdictions with different tax rates. Accordingly, the provision for income taxes does not necessarily equal the Canadian statutory rate. In fiscal 1998, the effective rate was significantly affected by the amortization of intangibles related to the acquisition of Accugraph, which are generally not tax deductible. Excluding the effect of the amortization of intangibles, the effective income tax rate for fiscal 1998 was 40.1%. This rate was lower than the Canadian statutory rate principally due to income being earned in jurisdictions with lower rates and the Ontario super allowance on research and development activity. The effective tax rate will continue to exceed the Canadian statutory rate during the period of amortization of intangibles associated with the Accugraph acquisition. Excluding the effect of this amortization, the tax rate should remain lower than the Canadian statutory rate as expansion continues outside of Canada to support foreign business opportunities.

LIQUIDITY

The Company ended the 1998 fiscal year in a highly liquid position, with working capital of $39.9 million, up from $36.5 million at the end of fiscal 1997 and $30.4 million at the end of fiscal 1996. The increase in working capital in fiscal 1998 and 1997 resulted from positive cash flows from operations. The increase in fiscal 1996 resulted mainly from the issuance of common shares in the Company's initial public offering for net proceeds of $30.6 million. From the proceeds of the initial public offering, a $3.0 million payment was made to the Company's bank to extinguish a demand installment loan incurred to make the royalty payment to NBTel. During fiscal 1998, the Company generated cash flows from operations, excluding changes in non-cash working capital items, of $9.9 million, up from $7.9 million in fiscal 1997 and $4.3 in fiscal 1996.

As at September 30, 1998, the Company's available funds consisted of approximately $31.0 million ($31.7 million at market value) in cash and short-term investments and $1.0 million in an unutilized revolving demand credit facility with a Canadian chartered bank. This facility is secured by a general security agreement covering all assets of the Company and a first charge on all intellectual property. This high level of liquidity is expected to continue throughout fiscal 1999, although it may be subject to minor fluctuations on a quarterly basis due to timing of cash receipts and disbursements. Excess funds are invested in highly rated Canadian federal or provincial government and corporate bonds (primarily denominated in Canadian dollars) with maturity dates generally ranging from 1 to 5 years. On assets held in the portfolio as at September 30, 1998, the average rate of return was approximately 6%. It is not the Company's intention to pay dividends in the foreseeable future.

Recently, the Company has financed its growth through cash from operations, proceeds from the initial public offering and, to a very limited extent in fiscal 1996, short-term bank borrowings. The Company believes that existing cash resources and available borrowings under its demand facility will be sufficient to meet its planned operating and capital expenditures for the foreseeable future.

No significant capital commitments exist; however, the Company has long term lease commitments as disclosed in Note 8 of the Notes to the Consolidated Financial Statements that relate principally to office facilities and computer equipment for research and development purposes.

In recent years, inflation has not had a material impact on the Company's operations.

CAPITAL EXPENDITURES

Capital expenditures increased by 81% to $3.4 million in fiscal 1998 from $1.9 million in fiscal 1997, which had declined 38% from expenditures of $3.1 million in fiscal 1996. The uneven timing of these expenditures reflects the deferral to fiscal 1998 of certain hardware and software purchases for research and development purposes. Otherwise these expenditures generally relate to additional office facilities, including the associated purchases of computer hardware and software, office equipment and furniture and fixtures, which were necessary to support significant growth in staff from 141 in September 1996 to 212 and 414 in September 1997 and 1998, respectively. Expenditures in fiscal 1998 reflect infrastructure increases, primarily in Toronto, to accommodate additional employees from the acquisition of Accugraph.

The Company anticipates that capital expenditures for fiscal 1999 will exceed those of fiscal 1998 due to continued investment in computer hardware and software for research and development purposes, further expansion of the Toronto head office, a new larger London office and potential additional European offices to support business opportunities.

MANAGING OPERATING RISKS

In addition to the potential for fluctuations in quarterly revenues and foreign exchange risks, discussed above, the significant operating risks facing the Company include maintaining revenue growth and expanding market share in an increasingly competitive market, maintaining the perceived technological superiority of its current products and completing the integration of these products, developing new products, and recruiting and retaining key personnel required to achieve these objectives.

HIGHLY COMPETITIVE MARKET

The market for OSSs remains highly competitive and is characterized by rapidly changing technologies, evolving industry standards, new product introductions and rapid changes in customer requirements. The Company expects this competition to increase. Key factors generally affecting the ability of the Company to compete are product functionality, performance and quality, product reputation, price, technical sales support, customer responsiveness and timely and cost effective implementation and delivery. The Company competes with systems integrators, telecommunications equipment vendors, hardware and software vendors and to a lesser extent with internal information systems departments of telecommunications companies. The Company competes with a number of companies that have substantially greater financial, technical, sales, marketing and other resources, as well as greater name recognition, than the Company. Some of these companies are able to offer financing options to end-users, putting the Company at a competitive disadvantage on these procurements. As a result, the competitors of the Company may be able to adapt more quickly to new or emerging technologies and changes in customer requirements, or to devote greater resources to the promotion and sale of their products than can the Company. Additional companies, including companies in the computer hardware, software and networking industries with significant market presence, may enter the provisioning market and further intensify competition. Competitive pressures may result in significant price erosion for the Company's products that could have a material adverse change on the Company's business, results of operations and financial condition. There can be no assurance that the Company will be able to compete successfully with its existing competitors or with new competitors.

NEW PRODUCTS AND TECHNOLOGICAL CHANGE

The Company believes that its recent success is in large part attributed to the superior functionality and performance of its products and that its ability to compete depends on maintaining this superiority. More recently, however, especially in the new entrant segment of the telecommunications service provider market, price and a more complete set of OSS solutions may be more important competitive factors than product superiority, as new entrants have limited financial and human resources and seek to deal with a limited number of independent solution providers. Furthermore, consolidation in the OSS industry is creating an ability on the part of some vendors to offer a broader suite of solutions. The acquisition of Accugraph was designed to address this need and to offer a suite of provisioning solutions; however, market demand may require an expansion of the product offering to include other related and unrelated OSSs. For this reason, and in order to sustain continued revenue growth, the longer-term success of the Company will be dependent upon not only maintaining the technological superiority of its current products, but also developing or acquiring additional OSS product solutions for the global telecommunications market. The Company's strategy is to continue to invest heavily in R&D to maintain the technological superiority of its current products, to integrate these products and to develop new products. The Company will also continue to assess potential acquisitions as a means of pursuing this strategy.

The Company's ability to enhance and integrate its existing products and to develop new products is in large part dependent upon relationships with key lead customers to assist in identifying requirements for such enhancements or products. The Company believes that it has such relationships, but the Company's business could be adversely affected if it incurs delays in developing new products or enhancements or if such products or enhancements do not gain market acceptance. In addition, there can be no assurance that products or technologies

developed by others will not render the Company's products or technologies non-competitive or obsolete. Furthermore, software products as complex as those to be offered by the Company may contain undetected errors or failures when first introduced or as new versions are released. There can be no assurance that, despite significant testing by the Company and by current and potential customers, errors will not be found in new products after commencement of commercial shipments. Such errors could result in loss of or delay in market acceptance.

RELIANCE ON STRATEGIC DISTRIBUTION PARTNERS

A significant factor in maintaining the Company's revenue growth in the short term is the ability of the Company to expand market penetration of its products, by market segment and geography, both directly and through sales channel partners. The Company's strategy is to increase its investment in its sales and marketing organization in order to enhance its direct sales capability in North and South America, Europe and Asia/Pacific as well as to make further investments to support existing and new strategic distribution partners. The Company cannot predict the extent to which its strategic distribution partners will be successful in marketing and selling the Company's products. Such sales channel partners have the capability to produce and some have in the past produced and continue to produce software or custom solutions competitive with the products of the Company. The Company's strategic distribution partners are not within its control, are not obligated to purchase products from the Company, and may also represent other vendors' product lines. There can be no assurance that these partners will continue their current relationships with the Company or that they will not give higher priority to the sale of other products, which could include products of competitors. The loss by the Company of, or the reduction in commitment by, any strategic distribution partner would have a material adverse effect on the Company's business, results of operations and financial condition and the inability to attract new strategic distribution partners could have a similar material adverse effect.

PRODUCT CONCENTRATION AND RELIANCE ON SIGNIFICANT CUSTOMERS

In recent years, the Company has derived a substantial portion of its revenues from the sale of ASAP. As a result of the acquisition of Accugraph during fiscal 1998, the Company currently derives revenues from three products and is currently developing a fourth product. These products are capable of being sold individually or as an integrated suite. Nevertheless, because of the related nature of these products, the Company remains subject to the risks of product concentration, and a decline in demand for these products, whether as a result of new competitive products, price competition, technological change, a decline in capital spending by service providers or other factors, could have a material adverse effect on the results of operations and financial condition of the Company.

As discussed above, a majority of the Company's total revenue in any year has been derived from large orders from a small number of customers and, during fiscal 1998, a significant portion of revenue was generated through one channel partner. In the foreseeable future, it is expected that a majority of revenues will also depend on large orders. Accordingly, the Company's future success depends in large part on its ability to develop new customer relationships with successful telecommunications service providers with sufficient financial and other resources.

OPERATIONS IN DEVELOPING COUNTRIES

Expansion of sales and operations into developing countries brings with it political and economic risks, unexpected changes in regulatory requirements, tariffs and other trade barriers, difficulties in staffing and managing foreign operations, complex local procurement practices and requirements, longer accounts receivable payment cycles and difficulties in enforcing rights in foreign courts. Fluctuations in foreign currency exchange rates could render the Company's products less competitive relative to local product offerings, or could result in foreign exchange losses, depending on the currency in which the Company sells its products. Although the Company intends to pursue sales opportunities in countries where these types of risks are greater, through strategic distribution partners, where feasible, there can be no assurance that such factors will not have a material adverse effect on the Company's revenues or its overall financial performance.

MANAGEMENT OF EXPANDING OPERATIONS

The Company has expanded its operations rapidly, including through the acquisition of Accugraph, which has placed significant demands on the Company's managerial, operational and financial personnel and systems. The Company intends to continue this rapid growth and the Company's future success depends on the ability of its officers and key employees to manage this rapid growth and changing business conditions effectively. The Company's future success also depends in large part on its key sales, marketing, product development and operational personnel, and its ability to continue to attract, motivate and retain highly qualified employees including technical, managerial and sales and marketing personnel. The employment market for such highly qualified personnel is highly competitive, putting upward pressure on compensation packages. The ability to issue stock options is an important factor in this regard.

RISKS ASSOCIATED WITH FUTURE ACQUISITIONS

In the normal course of its business, the Company evaluates potential acquisitions of businesses, products and technologies that would complement or expand its business. There can be no assurance that the Company will be able to successfully negotiate, finance or integrate any such acquired businesses, products or technologies. Furthermore, acquisitions may result in the diversion of management's attention from day-to-day operations and may include numerous other risks, including difficulties in the integration of operations, products and personnel, which if not undertaken effectively, efficiently and in a timely manner could have a material adverse effect on the Company's business, results of operations and financial condition. Acquisitions have the potential to result in dilutive issuances of equity securities, the incurring of additional debt, and amortization expenses related to goodwill and other intangible assets.

RELIANCE ON PROPRIETARY TECHNOLOGY AND THIRD PARTY SOFTWARE

The Company's success is also heavily dependent upon proprietary technology. The Company relies principally upon copyright protection and its trade secrets program to protect its proprietary technology. There can be no assurance that the steps taken by the Company in this regard will be adequate to prevent misappropriation or independent third-party development of its technology. Although the Company believes that its products and technology do not infringe patents or other proprietary rights of others, there can be no assurance that third parties will not claim the Company's current or future products infringe the patents or other proprietary rights of others. Such a claim, even if ultimately determined to be unwarranted, could result in litigation and temporary restrictions on the sale of the Company's products.

The Company also relies on certain software that it licenses from third parties, generally on a non-exclusive basis, including software that is integrated with internally developed software and used in the Company's products to perform certain key functions. There can be no assurance that such third party software licenses will continue to be available to the Company on commercially reasonable terms or at all. In addition, the Company is dependent upon such third parties' ability to enhance their current products and develop new products on a timely and cost effective basis that will meet changing customer needs and respond to emerging industry standards and other technological changes. There can be no assurance that the Company would be able to replace the functionality provided by third party software currently used in their respective products in the event such software were to become obsolete or incompatible with future versions of the Company's products. The loss or inability to maintain any of these software licenses or the inability of the third parties to timely and cost-effectively enhance their products could result in delays or reductions in product shipments by the Company, until equivalent software could be developed internally or identified, licensed and integrated, all of which could have a material adverse effect on the business, results of operations and financial condition of the Company.

Software licensed from third parties could also contain design defects or software errors that are difficult to detect or correct. The occurrence of errors or failures in software licensed from third parties could significantly impair the functionality, performance or operation of the Company's products. Furthermore, there can be no assurance that the third party software provider would be able to successfully correct such errors in a timely manner or at all. The consequences of such errors or failures could have a material adverse effect on the business, results of operations and financial condition of the Company.

YEAR 2000

Many currently installed computer systems and software products are coded to accept only two-digit entries in the date code field. Beginning in the year 2000, these date code fields will need to accept four-digit entries to distinguish 21st century dates from 20th century dates (the "Year 2000 Issue"). The Company has established a comprehensive project designed to identify and assess the impact of the Year 2000 Issue on its products, information technology systems, facilities and suppliers. The Company has targeted June 30, 1999 as the target date for completion of these efforts, which includes (i) assessment, (ii) remediation, (iii) testing and development of contingency plans, and (iv) implementation. The Company has completed the first two stages and is now in the testing phase. Based on the current assessment and representations from suppliers of internal systems and programs, the Company believes that such systems and programs either currently address the Year 2000 Issue, will be upgraded in the normal course and within the scheduled time frame to address the Year 2000 Issue, or, if necessary, can be replaced at no material additional cost to the Company. Other than seeking representations or assurances, the Company has not made any independent assessment as to whether any of its service providers will be affected by the Year 2000 Issue.

The Company also has a program to make its commercially available software products Year 2000 ready. ASAP, Objectel and Accugraph legacy products have all been tested for Year 2000 compliance and are generally available to customers. OMS and the Company's OSS interconnection gateway product, are scheduled to be tested for Year 2000 compliance and be generally available by June 1999. This includes ensuring proper interoperability with related data base and operating system software, as well as embedded third party software. The efforts to address the Year 2000 Issue are being performed as part of normal development activity and are not expected to result in any material incremental costs to the Company. Further modifications and testing of these products may be necessary, however, as a result of further changes to related third party products. The Company believes that it has sufficient resources to provide timely support to its customers implementing product upgrades. The Company's FAMIS product is not designed to address the Year 2000 Issue. The Company believes that it has no contractual or other obligation to modify the FAMIS product to address the Year 2000 Issue. The Company believes that all of its FAMIS customers will be replacing their FAMIS installations prior to December 31, 1999. Accordingly, the Company believes that it will incur no material cost or liability with respect to the Year 2000 Issue as it relates to its FAMIS product.

The Company believes that it is taking the necessary steps to resolve Year 2000 Issues and that its Year 2000 transition will be effected without material adverse impact on its business, operations, products or financial prospects. There can be no assurances, however, that despite the Company's efforts, it will not experience serious unanticipated negative consequences and/or material costs caused by undetected errors or defects in the technology used in its internal systems or those of its suppliers, in embedded software or related data bases or operating systems or in the Company's own products.

Certain parts of the foregoing discussion and analysis may be forward-looking statements that involve a number of risks and uncertainties. As a consequence, actual results may differ materially from results forecast or suggested in any forward-looking statements. Additional information on risks and uncertainties is contained in the Company's Annual Information Form as filed with the securities regulatory authorities in Canada and the United States.

management's responsibility for financial reporting

The accompanying financial statements and the information contained in this annual report are the responsibility of management and have been approved by the Board of Directors. Financial and operating data elsewhere in this annual report are consistent with the information contained in the financial statements.

These financial statements and all other information have been prepared by management in accordance with accounting principles generally accepted in Canada. Some amounts included in the financial statements are based on management's best estimates and have been derived with careful judgment.

In fulfilling its responsibilities, management has developed and maintains a system of internal controls. These controls ensure that assets are safeguarded from loss or unauthorized use and that financial records are reliable for the purpose of preparing financial statements. The Board of Directors carries out its responsibility for the financial statements through the Audit Committee which consists of non-management directors. The Audit Committee periodically reviews and discusses financial reporting matters with the Company's auditors, Deloitte & Touche, as well as with management.

The financial statements have been audited by Deloitte & Touche, Chartered Accountants.

ANTHONY P. VAN MARKEN
President and Chief Executive Officer

E. STUART GRIFFITH
Vice President, Finance and General Counsel

TO THE SHAREHOLDERS OF ARCHITEL SYSTEMS CORPORATION

We have audited the consolidated balance sheets of Architel Systems Corporation as at September 30, 1998 and 1997 and the consolidated statements of income and retained earnings and changes in financial position for the years then ended. These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at September 30, 1998 and 1997 and the results of its operations and the changes in its financial position for the years then ended in accordance with generally accepted accounting principles.

Deloitte & Touche LLP

CHARTERED ACCOUNTANTS
Toronto, Ontario
November 9, 1998, (except Note 14 (j), which is as of January 22, 1999)

auditor's report

consolidated balance sheets

	September 30 1998	September 30 1997
ASSETS		
Current		
Cash and short term investments	$ 30,981,935	$ 34,186,808
Accounts receivable (Note 2)	23,970,610	8,269,941
Investment tax credit recoverable (Note 3)	1,369,924	599,846
Prepaid expenses	599,307	262,198
	56,921,776	43,318,793
Capital assets (Note 4)	5,701,595	3,562,392
Deferred income taxes	731,120	528,180
Intangibles (Note 12)	32,359,664	–
	$ 95,714,155	$ 47,409,365
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	$ 12,951,833	$ 2,793,779
Income taxes payable	2,193,123	2,264,727
Deferred revenue	1,921,376	1,809,431
	17,066,332	6,867,937
Shareholders' equity		
Share capital (Note 5)	39,459,747	32,329,872
Contributed surplus (Note 5)	28,655,744	–
Retained earnings	10,532,332	8,211,556
	78,647,823	40,541,428
	$ 95,714,155	$ 47,409,365

Approved by the Board — *Director* — *Director*

consolidated statements of income and retained earnings

	Years ended September 30	
	1998	1997
Revenue		
License fees	$ 26,407,285	$ 20,890,284
Services and other	24,367,897	12,144,152
	50,775,182	33,034,436
Cost of sales		
License fees	574,790	–
Services and other	14,650,385	8,471,955
	15,225,175	8,471,955
Gross profit	35,550,007	24,562,481
Operating expenses		
General and administrative	5,708,263	4,732,439
Research and development (Note 3)	9,823,167	6,988,545
Sales and marketing	8,713,131	5,488,040
Royalties	–	1,987,700
	24,244,561	19,196,724
Income before interest income, amortization of intangibles and income taxes	11,305,446	5,365,757
Interest income	1,958,699	1,773,090
Amortization of intangibles	(5,620,369)	–
Income before income taxes	7,643,776	7,138,847
Income taxes (Note 6)	5,323,000	2,913,000
Net income for the year	2,320,776	4,225,847
Retained earnings, beginning of year	8,211,556	3,985,709
Retained earnings, end of year	$ 10,532,332	$ 8,211,556
Earnings per share (Note 6)		
Basic	$ 0.17	$ 0.34
Fully diluted	$ 0.17	$ 0.32

consolidated statements of

changes in financial position

	Years ended September 30	
	1998	1997
NET INFLOW (OUTFLOW) OF CASH RELATED TO THE FOLLOWING ACTIVITIES:		
Operating		
Net income for the year	**$ 2,320,776**	$ 4,225,847
Add back: items not affecting cash		
Amortization - capital assets	**2,147,113**	1,548,515
- royalty	**–**	1,912,700
- intangibles	**5,620,369**	–
Deferred income taxes	**(202,940)**	166,060
	9,885,318	7,853,122
Change in non-cash working capital items	**(11,086,706)**	448,684
	(1,201,388)	8,301,806
Investing		
Acquisition of Accugraph Corporation (Note 12)	**(34,349,530)**	–
Purchase of capital assets	**(3,439,574)**	(1,902,365)
	(37,789,104)	(1,902,365)
Financing		
Issuance of common shares	**35,785,619**	70,770
Net cash inflow (outflow)	**(3,204,873)**	6,470,211
Cash and short-term investments, beginning of year	**34,186,808**	27,716,597
Cash and short-term investments, end of year	**$ 30,981,935**	$ 34,186,808

1. ACCOUNTING POLICIES

These consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada and include the accounts of the Company and its wholly-owned subsidiaries. Amounts are expressed in Canadian dollars.

Cash and short term investments

Cash and short term investments consist of cash and fixed income investments. short term investments are carried at the lower of amortized cost and market.

Capital assets

Capital assets are stated at cost less accumulated amortization.

Amortization is recorded using the following rates and methods:

Computer equipment	-	2 years straight-line
Computer software	-	2 years straight-line
Furniture and equipment	-	20% per annum declining balance
Leasehold improvements	-	Over term of lease

Intangibles

Intangible assets include amounts allocated to the fair value of customer lists, research and development in process, acquired technology, and goodwill on acquisition. These intangibles are being amortized on a straight-line basis over their estimated useful lives as follows:

Customer lists	-	9 months
Research and development in process	-	18 months
Acquired technology	-	24 months
Goodwill	-	24 months

The Company regularly reviews the carrying values of intangibles to assess their recoverability from future earnings. If recoverability is not assured, the intangibles are written down to their net recoverable value.

Income taxes

The Company provides for income taxes based on accounting income using the deferral method. Deferred income taxes primarily comprise the difference between the accounting and tax value of capital assets, and the tax benefits arising from the Company's initial public offering. Under this method, taxes are computed using current tax rates regardless of when such income is subject to taxes under tax laws. The resulting deferred tax balances, are not adjusted for any subsequent changes in tax rates.

Recognition of revenue

License fees are generally recognized using either the percentage of completion method or on a contract milestone basis. The percentage of completion method is generally used where significant development of the licensed software product is required, or when acceptance of the licensed software product is dependent upon acceptance of related services. Recognition on contract milestones generally applies where minimal or no development of the licensed software product is required. Where the percentage of completion method is used, revisions to cost and profit estimates made during the course of work are reflected in the period in which the change is known. Provision is made in full for any anticipated loss when the estimate of total costs on a contract indicates a loss.

Services and other revenue, which consists of professional services revenue, product support revenue, and commissions earned from a third party software vendor, is recognized in the period in which the work is performed or commission earned. Certain contracts contain incentive provisions based on achieving performance milestones. These awards are included in income when realized.

Deferred revenue represents billings in advance of the services provided.

Accrued revenue for contracts in progress, included under accounts receivable, represents goods and services delivered or performed but not billed.

Research and development costs and investment tax credits

Research costs are expensed as incurred.

Development costs are expensed as incurred unless they meet the generally accepted accounting criteria for deferral and there is reasonable assurance they will be recovered. In the two years ended September 30, 1998, all development costs have been expensed as incurred.

Investment tax credits are recognized as a reduction of research and development costs when there is reasonable assurance that they will be realized.

Use of Accounting Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires the Company's management to make estimates that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods presented. In particular, revenue recognition using the percentage of completion method requires the use of estimates of costs to complete projects. Actual results could differ from the estimates made by management.

Foreign currency translation

The financial statements of the Company's foreign subsidiaries, all of which are considered to be operationally dependent upon the Company, are translated using the temporal method. Under this method, revenues and expenses are translated at rates in effect on the transaction date. Monetary assets and liabilities are translated at the rate of exchange at the balance sheet date. Non-monetary assets and liabilities are translated at historical exchange rates. Exchange gains and losses on translation are included in the Consolidated Statements of Income under General and Administrative expenses.

2. ACCOUNTS RECEIVABLE

	1998	1997
Billed receivables	$ 14,002,101	$ 3,566,859
Accrued revenue for contracts in progress	9,968,509	4,703,082
	$ 23,970,610	$ 8,269,941

3. INVESTMENT TAX CREDIT RECOVERABLE

For the year ended September 30, 1998, investment tax credits in the amount of $585,000 (1997 - $283,000) have been recognized as a reduction of research and development expenses.

4. CAPITAL ASSETS

1998	Cost	Accumulated Amortization	Net Book Value
Computer equipment	$ 3,803,010	$ 2,819,926	$ 983,084
Computer software	2,948,307	1,701,196	1,247,111
Furniture and equipment	2,913,250	893,078	2,020,172
Leasehold improvements	1,822,080	370,852	1,451,228
	$ 11,486,647	$ 5,785,052	$ 5,701,595

1997	Cost	Accumulated Amortization	Net Book Value
Computer equipment	$ 2,734,355	$ 1,890,430	$ 843,925
Computer software	1,600,580	998,295	602,285
Furniture and equipment	1,753,310	554,307	1,199,003
Leasehold improvements	1,112,085	194,906	917,179
	$ 7,200,330	$ 3,637,938	$ 3,562,392

5. SHARE CAPITAL

Authorized
- Unlimited number of common shares
- Unlimited number of preferred shares, issuable in series

Changes to issued share capital are as follows:

	Number of Common Shares	Amount
Issued and outstanding at September 30, 1996	12,340,144	$ 32,259,102
Issue of shares for cash under the Flexible Share Incentive Plan, net of repurchases	215,400	64,620
Issue of shares for cash under the 1996 Stock Option Plan	750	6,150
Issued and outstanding at September 30, 1997	12,556,294	32,329,872
Issue of shares for cash under the Flexible Share Incentive Plan, net of repurchases	54,800	16,440
Issue of shares for cash under the 1996 Stock Option Plan	212,844	1,916,859
Issue of shares on acquisition of Accugraph Corporation	2,246,040	5,011,840
Issue of shares for cash under the Accugraph Corporation 1996 Stock Option Plan	10,832	159,335
Issue of shares for cash under the Accugraph Key Employee Stock Option Plan	1,803	25,401
Issued and outstanding at September 30, 1998	15,082,613	$ 39,459,747

(a) Contributed surplus of $28,655,744 includes the excess of the share consideration over the stated share capital on the acquisition of Accugraph Corporation (Note 12) in the amount of $27,555,744, and the tax benefit from US employees exercising stock options in the amount of $1,100,000.

notes financial statements

(b) The Company has adopted, or assumed in the Accugraph acquisition, the following stock incentive arrangements, under which options to purchase shares have been granted to directors, officers, employees and/or consultants:

(i) the Flexible Share Incentive Plan;
(ii) the 1996 Stock Option Plan;
(iii) the Accugraph Corporation 1992 Directors and Officers Stock Option Plan;
(iv) the Accugraph Corporation Key Employee Stock Option Plan; and
(v) the Accugraph Corporation 1996 Stock Option Plan.

Options outstanding under the Accugraph plans, as at the acquisition date, were converted to equivalent options to purchase Architel shares using an exchange ratio of 0.0833 of an Architel share for every Accugraph share, with an equivalent adjustment to the exercise price.

The following options are outstanding as at September 30, 1998:

	Options Outstanding	Weighted Average Exercise Price
Flexible Share Incentive Plan	64,400	$ 0.30
1996 Stock Option Plan	1,519,002	11.85
Accugraph Corporation 1992 Directors and Officers Stock Option Plan	5,831	35.99
Accugraph Corporation Key Employee Stock Option Plan	23,548	31.78
Accugraph Corporation 1996 Stock Option Plan	79,874	14.76
	1,692,655	$ 11.91

Subsequent to September 30, 1998, the Company issued additional options to purchase common shares under the 1996 Stock Option Plan as follows:

Date of Grant	**Number of Options**	**Exercise Price**
October 1, 1998	**193,103**	**$ 9.70**
November 1, 1998	**34,250**	**$ 14.75**
Total	**227,353**	

In addition to the number of options outstanding at September 30, 1998 and granted subsequent to year end, 532,130 options are available for future issuance under the 1996 Stock Option Plan. No further options will be issued under any of the other plans.

Options under the Flexible Share Incentive Plan were granted in January 1995, are fully vested as at September 30, 1998 and can be exercised until January 1, 2005. Options under the 1996 Stock Option Plan are granted with an exercise price not less than the market price of the common shares at the date of grant, generally vest over a three or four year period from the date of grant and expire 10 years from the date of grant. Options under the Accugraph Corporation 1992 Directors and Officers Stock Option Plan are fully vested as at September 30, 1998 and have a variety of expiry dates ending no later than May 2001. Options under the Accugraph Corporation Key Employee Stock Option Plan have a variety of vesting schedules and expiry dates ending no later than January 2002. Options under the Accugraph Corporation 1996 Stock Option Plan have a variety of vesting schedules and expiry dates ending no later than April 2005.

6. INCOME TAXES

	1998	1997
Current	**$ 5,742,000**	$ 2,963,000
Deferred	**(419,000)**	(50,000)
	$ 5,323,000	$ 2,913,000

Income tax expense, including both the current and deferred portions, varies from amounts which would be computed by applying the Company's combined statutory income tax rate as follows:

	1998	1997
Combined rate of income taxes at 44.62% (1997 - 44.62%)	**$ 3,411,000**	$ 3,185,000
Increase (decrease) resulting from:		
Amortization of intangibles	**2,506,000**	-
Other permanent differences	**85,000**	52,000
Effect of lower tax rate on foreign income	**(310,000)**	(200,000)
Benefit of loss carry forward	**(257,000)**	-
Other	**(112,000)**	(124,000)
	$ 5,323,000	$ 2,913,000

At September 30, 1998, the Company had accumulated losses and timing differences for tax purposes of approximately $800,000 which have not been recognized in these financial statements, and are available to be applied against future taxable income until 2004.

7. EARNINGS PER SHARE

Basic earnings per share are calculated using the weighted monthly average number of common shares outstanding during the year.

Fully diluted earnings per share are calculated under the assumption that all dilutive share options outstanding at the end of the year had been exercised at the later of the beginning of the year and the date of grant.

8. COMMITMENTS AND CONTINGENCIES

(a) The Company and its subsidiaries have obligations under long-term leases for office facilities and equipment. The future minimum lease payments under these operating leases are as follows:

1999	$ 3,315,259
2000	2,658,433
2001	2,238,327
2002	1,934,342
2003	1,819,473
Thereafter	2,092,377

(b) The Company and its subsidiaries face the possibility of routine litigation incidental to its business, and to assessment and reassessment of income and other taxes by various taxing authorities. The Company believes it has provided adequately for these matters and accordingly their ultimate disposition will not have a material affect on its consolidated earnings or financial position.

9. LINE OF CREDIT

The Company has an available line of credit of $1,000,000 with its bankers that is secured by accounts receivable, a general security agreement and a specific first charge over intellectual property. As at September 30, 1998, no amounts were drawn on this facility.

10. SEGMENTED INFORMATION

The Company operates principally in the design, development and support of advanced operations support systems for the global telecommunications industry. The results of the Company's operations are not measured by country or region, accordingly geographic segments have not been provided. The distribution of sales by ultimate customer is as follows:

	1998		1997	
Canada	**$ 6,330,000**	**12.5%**	$ 2,233,000	6.8%
United States and Carribean	**28,604,000**	**56.3%**	29,333,000	88.8%
Europe	**14,929,000**	**29.4%**	877,000	2.7%
Asia Pacific	**912,000**	**1.8%**	591,000	1.8%
	$ 50,775,000	**100.0%**	$ 33,034,000	100.0%

11. FINANCIAL INSTRUMENTS AND CONCENTRATION OF CREDIT RISK

The carrying value for all financial instruments approximate fair value with the following exception:

	1998		1997	
	Carrying Value	**Fair Value**	Carrying Value	Fair Value
Financial Assets				
Cash and short term investments	**$ 30,981,935**	**$ 31,705,363**	$ 34,186,808	$ 35,177,937

The estimated fair values of cash and short term investments include the unrealized gains on investments held. The estimates are not necessarily indicative of the amounts the Company could potentially realize in a current market exchange.

financial statements

Foreign Exchange Risk

The Company maintains its accounts in Canadian dollars. However a portion of its operations are located in other foreign jurisdictions, and its products are priced in foreign currencies. Therefore, the Company is subject to foreign currency fluctuations which may, from time to time, affect its profitability and cash flow.

Interest Risk

Surplus cash is invested according to the Company's investment policy, which states the primary objective as the preservation of capital. Investment credit risk is managed by limitations on the grade of securities, diversification of issuers and limitations on terms to maturity. The Company is subject to interest rate risk in the form of varying rates of return on its investment portfolio.

Credit Risk

Accounts receivable from four customers represents 59% of total accounts receivable at September 30, 1998 (1997 — two customers represented 65%). The Company believes that there is minimal risk associated with the collection of these amounts, as such amounts are receivable from large established telecommunication companies. The balance of accounts receivable is widely distributed among other customers.

12. ACQUISITION

On June 29, 1998 the Company acquired all of the issued and outstanding shares of Accugraph Corporation (a Canadian Corporation), pursuant to a plan of arrangement between the Company and the holders of the aforementioned shares. The acquisition is being accounted for under the purchase method of accounting, and as such the consolidated statements of income include the results of operations from the date of acquisition. Accugraph Corporation's business included the development, sale and support of operations support systems used in the global telecommunications industry.

As consideration, the Company issued 2,246,040 common shares valued at $14.50 per share, being an average of the market value of the Company's common shares over the period immediately prior to June 29, 1998.

The purchase price was determined as follows:

Share consideration given	$ 32,567,584
Transaction and integration costs	1,781,946
	$ 34,349,530

The purchase price was allocated as follows:

Current assets	$ 6,705,674
Non-current assets	627,742
Liabilities	(10,963,919)
Customer lists	1,097,920
Research and development in process	11,335,440
Acquired technology	18,166,780
Goodwill	7,379,893
	$ 34,349,530

As at September 30, 1998, there was accumulated amortization of intangibles totaling $5,620,369.

13. YEAR 2000

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. The effects of the Year 2000 Issue may be experienced before, on, or after January 1, 2000, and, if not addressed, the impact on operations and financial reporting may range from minor errors to significant systems failure which could affect an entity's ability to conduct normal business operations. It is not possible to be certain that all aspects of the Year 2000 Issue affecting the Company, including those related to the efforts of customers, suppliers, or other third parties, will be fully resolved.

14. UNITED STATES ACCOUNTING PRINCIPLES

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"), which conform in all material respects, with those in the United States ("U.S. GAAP") during the periods presented except with respect to the following:

(a) The definition of cash used in the accompanying statements of changes in financial position includes cash and short term deposits. Under U.S. GAAP, cash would exclude short term deposits with original maturities in excess of 90 days. Changes in short term deposits with original maturities in excess of 90 days would be presented as investing activities. Under U.S. GAAP, for the years ended September 30, 1998 and 1997, cash as defined above would be $3,666,926 and $7,634,295 respectively. Cash used in investing activities would increase by $762,496 and $1,565,649 respectively.

(b) Under Canadian GAAP, there is no requirement to record compensation on the issue of stock options to employees, consultants or directors. Under U.S. GAAP APB No. 25, compensation equal to the difference between the market price of the stock and the exercise price of the option is recorded as an expense over the period of vesting of the option, with a corresponding increase to additional paid in capital, a component of shareholders' equity. Accordingly, for U.S. GAAP purposes, for the years ended September 30, 1998 and 1997, net income would be decreased by $715,648 and $749,257 respectively. The compensation effect on fiscal years prior to 1997 would result in a decrease in retained earnings of $2,065,570 and an increase in additional paid in capital of $2,065,570. Additional paid in capital would be increased by $3,530,475 at September 30, 1998, and $2,814,827 at September 30, 1997.

(c) In accordance with Canadian GAAP, it is the Company's policy to capitalize and amortize acquired in process research and development. Under U.S. GAAP, acquired in process research and development is expensed. Therefore, for U.S. GAAP purposes, for the years ended September 30, 1998 and 1997, amortization of intangibles would increase by and net income would decrease by $9,321,474 and $nil respectively.

(d) The following additional disclosures are required in the financial statements under U.S. GAAP:

- (i) Interest paid during the years ended September 30, 1998 and 1997, was $38,658 and $ nil respectively.
- (ii) Allowances for doubtful accounts on accounts receivable as at September 30, 1998 and 1997, are $1,622,591 and $22,255 respectively.
- (iii) Accrued liabilities and other non-trade payables included in accounts payable as at September 30, 1998, and 1997, are $10,504,262 and $2,319,147 respectively.
- (iv) Foreign exchange gains for the years ended September 30, 1998 and 1997, are $1,071,751 and $116,590 respectively.
- (v) Investment tax credits which were credited to research and development expenses under Canadian GAAP would instead be credited to the income tax provision under U.S. GAAP. For the years ended September 30, 1998 and 1997, $585,000 and $283,000 respectively would be credited to the income tax provision.

(e) Under U.S. GAAP, the Company would have adopted the SFAS No. 109, Accounting for Income Taxes. In accordance with SFAS No. 109, income taxes reflect the impact of net operating loss carry forwards, general business credit carry forwards, and temporary differences between values recorded for assets and liabilities for financial reporting purposes and values utilized for measurement in accordance with income tax laws. Under Canadian GAAP, tax benefits would arise from US employees exercising stock options for the years ended September 30, 1998 and 1997 in the amounts of $1,100,000 and $nil, respectively, and have been included in contributed surplus. Under U.S. GAAP, $nil and $205,000 for 1998 and 1997, respectively, would have been recorded as adjustments to additional paid in capital. In addition, under U.S. GAAP, the benefit of loss carry forwards not previously recognized on acquisition would result in an adjustment to goodwill. During the most recent period, tax benefits of $257,000 in excess of those recorded at the acquisition date were realized.

(f) In June 1997, the Financial Accounting Standards Board issued SFAS No. 130, Reporting Comprehensive Income. Implementation of SFAS 130 is required for the Company's 1999 fiscal year. SFAS 130 establishes standards for the reporting of all components of comprehensive income. The Company will adopt the provisions of SFAS No. 130 on a comparative basis.

In June 1997, the Financial Accounting Standards Board issued SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information. Implementation of SFAS 131 is required for the Company's 1999 fiscal year. SFAS 131 redefines how operating segments are determined and requires disclosure of certain financial and descriptive information regarding those segments. The Company continues to evaluate the impact of the new requirement.

Note to RA - please give this one to Sandy

(g) The following table reconciles net income for the years in accordance with U.S. GAAP:

		Years ended September 30, 1998		Years ended September 30, 1997
Net income in conformity with Canadian GAAP		$ 2,320,776		$ 4,225,847
Adjustments:				
Additional compensation re stock options	65	(715,648)	FAS 123, APB 25	(749,257)
Tax benefit of loss carry forward	8	(257,000)	FAS 109	–
Acquired research and development in process	34	(9,321,474)	In-process R&D	
		(10,294,122)		
Net income (loss) in conformity with U.S. GAAP		$ (7,973,346)		$ 3,476,590
Basic earnings (loss) per common share - U.S. GAAP		$ (0.61)		$ 0.28
Diluted earnings (loss) per common share - U.S. GAAP		$ (0.61)		$ 0.28

Earnings per common share is determined using the weighted average number of shares outstanding during the period. Diluted earnings per common share reflect the dilutive effects of the common share options outstanding at the end of the period.

(h) The following table indicates the items in the balance sheet that would be affected had the financial statements been prepared in accordance with U.S. GAAP:

Call to phone the company

	As at September 30, 1998	As at September 30, 1997
Cash	$ 3,666,926	$ 7,634,295
Short term investments	27,315,009	26,552,513
Intangibles	22,781,190	–
Accounts payable	2,447,571	474,632
Accrued liabilities	10,504,262	2,319,147
Deferred income tax assets	731,120	1,570,180
Retained earnings (deficit)	(2,576,617)	5,396,729
Additional paid in capital	4,572,475	3,856,827

(i) Supplementary Income Statement Information

	Years ended September 30, 1998	Years ended September 30, 1997
Advertising and marketing costs	$ 2,969,988	$ 759,784
Taxes, other than payroll and income taxes	24,500	100,810
Income taxes paid	3,500,000	800,000

65 (593,456)
8 (93,119)
34 (7,739,899)

(j) Subsequent to September 30, 1998, the Company's management revised its allocation of value to assets acquired from Accugraph. Specifically, the Company changed the methodology used to value the technologies acquired, to adopt a methodology which it understands is consistent with recent regulatory guidelines. As a result of this change in methodology, the amounts allocated to research and development in process, acquired technology and goodwill have been revised. These consolidated financial statements and related notes reflect these revised valuations.

p. 30	CAN GAAP	Am GAAP	Diff	
R.E.	10,532,332	(2,576,617)	(13,108,949)	Book value (OE) ↓
Additional Paid in Capital	0	4,572,475	4,572,475	Book value of (OE) ↑
			(8,536,474)	

Book value of OE lower → by the 8,536,374
Pro-rate the I/S differences above

corporate **information**

market leader growth new frontier market leader vision growth frontier growth

BOARD OF DIRECTORS

ANTHONY P. VAN MARKEN
President and Chief Executive Officer

PAUL DAMP (1)(2)
Chairman
Chairman, Kestrel Capital Partners

DAVID E. CURRY
Senior Vice President, Business Development

JOHN MCLENNAN (1)(3)
President, Jenmark Consulting

ROY D. TRIVETT (4)
Private Consultant

(1) Member of Audit Committee
(2) Member of Compensation Committee
(3) Chairman of Compensation Committee
(4) Chairman of Audit Committee

CORPORATE OFFICERS

ANTHONY P. VAN MARKEN
President and Chief Executive Officer

DAVID E. CURRY
Senior Vice President, Business Development

ROBERT W. FILLMORE
Vice President Sales, Europe, Middle East, Africa (EMEA)

E. STUART GRIFFITH
Vice President, Finance and General Counsel

RICHARD KATHNELSON
Vice President, Human Resources

DAVID W. NYLAND
Vice President, Worldwide Professional Services

ZARAR RANA
Senior Vice President, Engineering

JOEL STRIMBAN
Vice President, Global Partner Alliances

PHILIP THRASHER
Vice President Sales, Americas

DANIEL K. VERMEIRE
Vice President, Marketing

CORPORATE DIRECTORY

AUDITORS
Deloitte & Touche LLP, Chartered Accountants, Toronto, Ontario

GENERAL COUNSEL
Fasken Campbell Godfrey, Toronto, Ontario

TRANSFER AGENT AND REGISTRAR
Investors are encouraged to contact CIBC-Mellon Trust Company for information regarding their security holdings. They can be reached at:

CIBC-Mellon Trust Company
393 University Avenue, 5th Floor
Toronto, Ontario, M5G 2M7

Answer line: (416) 813-4600 or toll free throughout North America at 1-800-387-0825

Internet address: www.rmtrust.ca (web site) or invcorr@rmtrust.ca (e-mail)

COMMON STOCK
Architel's common stock is traded on The Toronto Stock Exchange in Canada under the symbol "ASY" and on the NASDAQ Stock Exchange in the United States under the symbol "ASYCF".

INVESTOR RELATIONS
For additional copies of this annual report, Architel's annual information form, quarterly reports, or for further information please contact Investor Relations.

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Canada M9W 6H8

Tel: (416) 674-4086
Fax: (416) 674-2290

email: investor_relations@architel.com

ANNUAL AND SPECIAL MEETING OF SHAREHOLDERS
The Annual and Special Meeting of Shareholders will be held at 3:00 p.m., Wednesday, March 24, 1999 at the:

Toronto Airport Hilton
The Dundas Room
5875 Airport Road
Mississauga, Ontario L4V 1N1

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